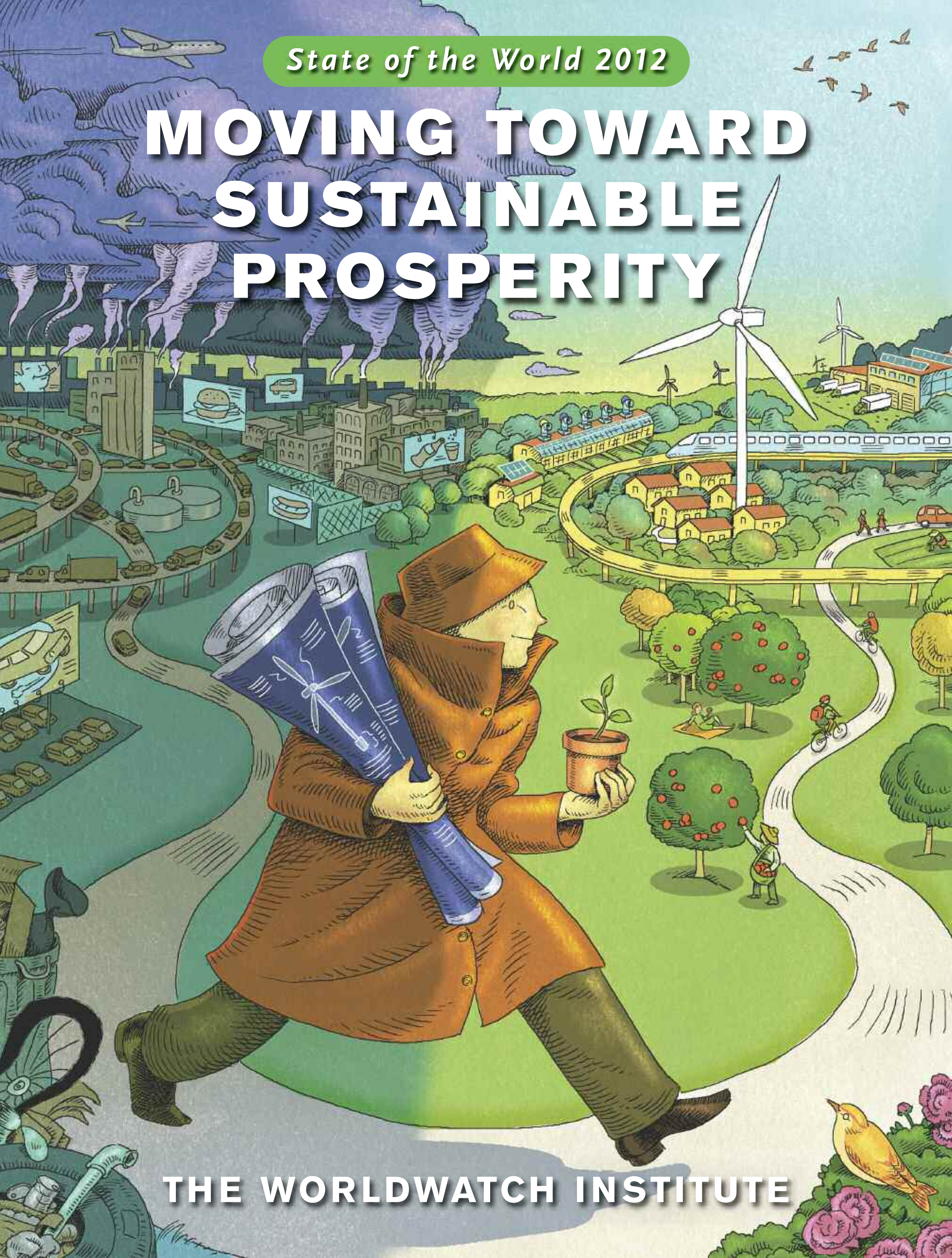
State of the World 2012

MOVING TOWARD SUSTAINABLE PROSPERITY



THE WORLDWATCH INSTITUTE

CHAPTER 7

Reinventing the Corporation

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In early 2011, U.N. Secretary-General Ban Ki-moon challenged the global community with these words: "We need a revolution. Revolutionary thinking. Revolutionary action…It is easy to mouth the words 'sustainable development,' but to make it happen we have to be prepared to make major changes—in our lifestyles, our economic models, our social organization, and our political life."[1]

The Secretary-General is not the first to call for such systemic change. But he, like virtually all others calling for deep change in the planet's development trajectory, left unanswered the critical question of change agent. Who possesses the vision, leadership, and capacity to galvanize the "revolution" leading toward a just and sustainable world during the turbulent decades that lie ahead?

Will leadership come from existing or new global governance bodies equipped with the legitimacy and authority to manage complex and urgent transnational issues such as climate change, responsible international financial regulation, and fair trade? What about civil society? Will it surmount its fragmentation and evolve into a cohesive force for transformational change beyond its contribution to issue-specific causes such as biodiversity, fair labor practices, and human rights? Is it plausible that a global citizens movement, diffuse and spontaneous yet bound together by common values, forms a social movement that mobilizes millions in support of a "Great Transition"?[2]

And what role for corporations, especially transnational corporations (TNCs) that have a position of global influence that rivals or exceeds the reach of other institutions on the global stage? While corporations by no means stand alone as the sole cause of multiple social and ecological crises, they indisputably play a prominent role in their creation and persistence. Consider the roles of financial institutions in the financial crisis, fossil fuel companies in climate change, and the advertising industry in unsustainable consumerism. Correcting such misalignments will require rethinking the fundamentals regarding societal needs and expectations in relation to corporate form and practices.

Any vision of the global future in the coming decades must include full recognition of the role TNCs play in shaping the planet's human and ecological destiny. It is this reality that animates the intense contemporary debates about the role of business in society and the

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capacity—and will—of corporations to simultaneously create public benefit alongside private wealth at a scale and speed commensurate with the needs of a struggling, perilous world. It is difficult, arguably impossible, to imagine a future of 9 billion people living sustainably in the absence of systemic change in the purpose and design of corporations.

Ascendance of Transnationalism

Five centuries ago, the precursor of the modern TNC appeared in the form of sixteenth-century government-chartered trading companies organized by the British and Dutch royalties. While centuries would pass before such global entities would reach the position of dominance now exercised by some 75,000 enterprises, the idea of transnational commerce was set in place by trading companies that functioned as agents of both political and economic domination of the early colonial powers. (See Box 7–1.)[3]

In those early forms, wealth was tied not to the production of goods but to service as brokers between sellers and buyers of spices, silks, minerals, and eventually human beings. The trading companies served to enrich the royalty and, years later, the investors whose capital enabled the expansion of trading activities in return for a share of the profits. The idea that owners of capital could reap the fruits of corporate activity began to take root, the beginning of a slow evolution toward shareholder primacy that centuries later would legitimize "shareholder value" as the core purpose of the modern corporation. Wealth dominated by landholding shifted to wealth accrued through trade enabled by private investors. The era of economic globalization began its slow but steady ascent to full fruition in the post–World War II era.

The march of TNCs toward ever increasing size and geographic reach continues unabated. This trend becomes evident through any number of measures. Employees in foreign affiliates of TNCs, for example, grew from 21.5 million in 1982 to 81.6 million in 2007. Sales by foreign affiliates increased from $2.7 trillion to $31.2 trillion over the same period—more than an 11-fold increase. Assets increased even more, from $2.2 trillion to nearly $69 trillion.[4]

Figure 7–1 offers a complementary perspective on this expansionist trend. Corporate functions abroad such as sales offices, logistics, call centers, and R&D all show increases between 2008 and 2011. Even corporate headquarters and other "decisionmaking centers" align with this trajectory. Perhaps most ominous from the standpoint of western nations is the movement of R&D functions out of home countries, signaling the growing capacity of emerging economies to participate actively in all aspects of the value chain, not just the traditional resource extraction, processing, and assembly functions long associated with that part of the world.[5]

The first decade of the twenty-first century is thus witnessing dramatic shifts in the global TNC landscape as many corporations seek locations closer to customers and talent in emerging markets. Principal among these is the emergence of TNCs headquartered in these countries, positioning themselves as competitors in the global economy based on scale, technological prowess, and typically a prominent government role in ownership, oversight, and subsidies.[6]

"State capitalism" of this nature is in itself a major force in the expansion of TNCs in Brazil, Russia, and China, driving firms such as SINOPEC, China National Petroleum, State Grid (China), Gazprom (Russia), and Petrobras (Brazil) to rank among the world's top 50 by revenues, with all exceeding $100 billion annually.[7]

As rapid growth in emerging economies continues in the coming decade, the competitiveness of such firms will be a major force in shaping the global future. Along the way, west-

Box 7–1. The Roots of the Modern Corporation

At the dawn of the eighteenth century, industrial production emerged as a new and more powerful source of wealth creation. This development was noteworthy not only for the emergence of the industry-based corporation but also for the shift from wealth dominated by inheritance and social status to wealth driven by entrepreneurship and production of manufactured goods. Innovation gradually displaced entitlement as the primary determinant of such wealth. An entrepreneurial class, fueled by increasing access to private capital, began to redefine the corporate landscape. This process marked the beginning of limited democratization of wealth within the narrow confines of the investor class that a century later would overtake royalty and nobility in terms of aggregate control of the world's wealth.

By the early nineteenth century, two major innovations in corporate form emerged as the dominant architecture that redefined the prevailing model. Until then, partnerships of a few private investors plus the entrepreneur controlled the corporation. In the early 1800s, with opportunities for commerce outstripping the capital available through private partnerships, companies turned to joint stock arrangements. Under this regime, investors large and small could partake in the surging opportunities spawned by industrialization by purchasing stock in the enterprise. Through stock exchanges, investors both near and far could buy shares without substantive involvement—or even knowledge—of how the company operated. Returns in the form of dividends and stock appreciation were enough to attract waves of capital from those seeking to profit from the industrialization that was sweeping Europe and North America.

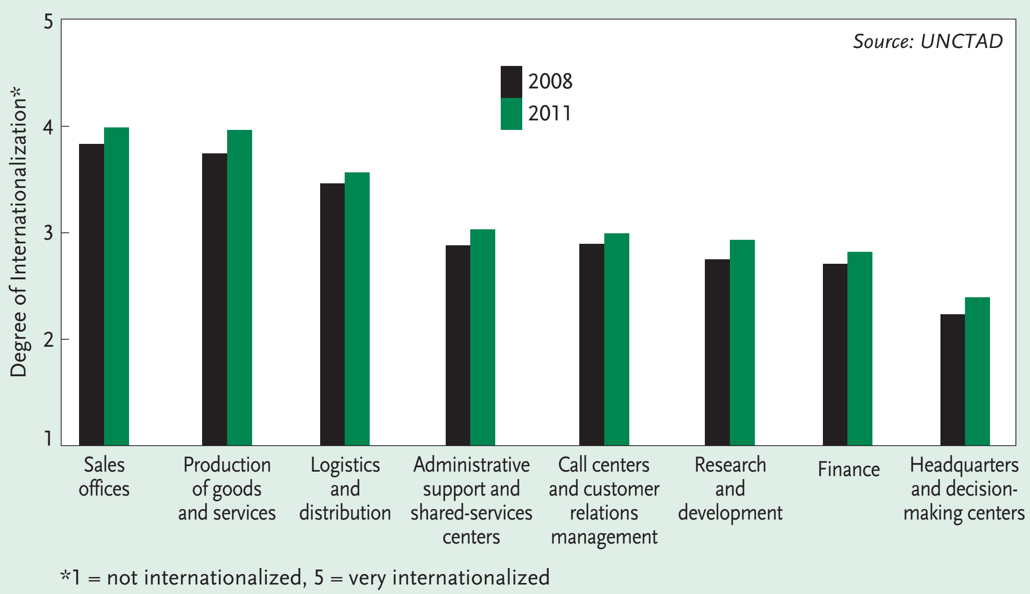
Along with joint stock ownership, the concept of "limited liability" redefined the nature of the corporation. Limited liability capped risk at a level equal to the value of the investor's shares in the organization, creating the prospect of unlimited gains with limited risk. Industrialists argued before governments that this arrangement was indispensable in order to keep capital flowing to expanding companies that, by the late nineteenth century, were emerging as the world's dominant corporate form.

The dual forces of joint stock and limited liability became the pillars of unprecedented growth in the size, complexity, and profitability of large corporations. The corporation as a remote, tradable asset held by anonymous investors decoupled from management, operations, and community took root. At the same time, labor as a factor of production akin to raw materials whose cost should be minimized became deeply embedded in the world's surging industrial economies.

These attributes put in place the defining characteristic of the modern corporation, namely the primacy of capital (that is, shareholder) interests. The ripple effects of this primacy flowed through every artery of the industrial economy. Conceived as mechanisms to attract money in an era of capital scarcity, shareholder primacy created conditions that would spur many of the social movements that pitted the rights of capital against the rights of labor. With the exceptions of the solidarity during World War II and the shared prosperity of the 1950–80 period, the friction between the rights of capital owners and the rights of labor remain, with varying intensity, a central feature of advanced economies to this day.

Source: See endnote 3.

Figure 7–1. Proportion of Corporate Functions Undertaken Abroad



ern standards of corporate governance, social responsibility, and ethics will not automatically become the norms of this new generation of TNCs. Indeed, the world view of the governments and executives that shape such enterprises already is bringing a strong element of sovereign interests in defining what constitutes fair play and responsible conduct in the twenty-first century.

Meanwhile, many other forces render forecasts decidedly uncertain: the availability and price volatility of mineral and food commodities as well as dramatic advances in information technologies and social networking are enabling popular campaigns against whole business sectors and individual companies. The result is rising pressure on business to deliver traditionally public goods such as education and health and, for those firms attuned to new market opportunities, to serve the poorest of the poor with affordable consumer goods and services. Taken together, all signs point to an era that will challenge sacred cows and prevailing beliefs that underlie the social contract between citizens, their governments, and the corporation—the new party to the bargain.[8]

The Emergence and Limitations of Soft Law

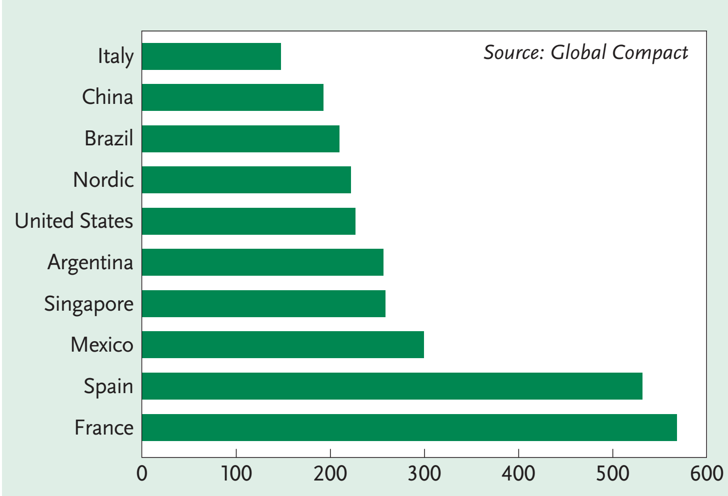
Against this dynamic backdrop, numerous initiatives in the field of corporate sustainability provide a glimpse of the evolving expectations that both reflect and shape new norms of corporate behavior. Most of these fall into the category of voluntary, externally driven efforts to shift corporate behavior toward alignment with the tenets of sustainability: intergenerational responsibility, environmental stewardship, and social justice. This category of initiatives has given rise to a body of "soft law" through which new norms of conduct emerge not through government mandate but

through voluntary actions triggered by nongovernmental and multilateral actors that, over time, build legitimacy and uptake outside any formal legislative or regulatory process.

Dozens of examples of voluntary initiatives have emerged in the last two decades. As such efforts multiply, many questions have arisen regarding their credibility and impact. Are such programs actually driving corporate conduct toward higher levels of social purpose? Is voluntarism enough to achieve transformational change leading to new norms and measureable outcomes aligned with sustainability? Are these efforts moving away from corporate forms anchored in profit maximization and shareholder enrichment? In short, are such initiatives too incremental and inherently incapable of addressing the urgent and interdependent environmental, social, and economic crises that threaten planetary well-being?[9]

The Global Compact launched in 1999 by U.N. Secretary-General Kofi Annan provides a telling example of the promise and limitations of voluntary initiatives. The Compact operates as a values platform and learning network to advance 10 principles of corporate conduct covering environment, labor standards, human rights, and anti-corruption. It was a historic moment when the world's leading international governmental body explicitly recognized that a just and sustainable future cannot emerge without serious engagement and concrete action on the part of the global business community. Self-described as the "world's largest corporate citizenship and sustainability initiative," some 8,000 participants, including approximately 6,000 corporate endorsers in 135 countries, subscribe to the 10 principles and commit to regular reporting on progress toward their implementation. Among corporate endorsers, about half are large companies and half small or medium-size enterprises (fewer than 250 employees). As measured by company headquarters, the countries most involved in the Compact are France, Spain, and Mexico. (See Figure 7–2.)[10]

Figure 7–2. Countries and Regions with Most Global Compact Company Headquarters

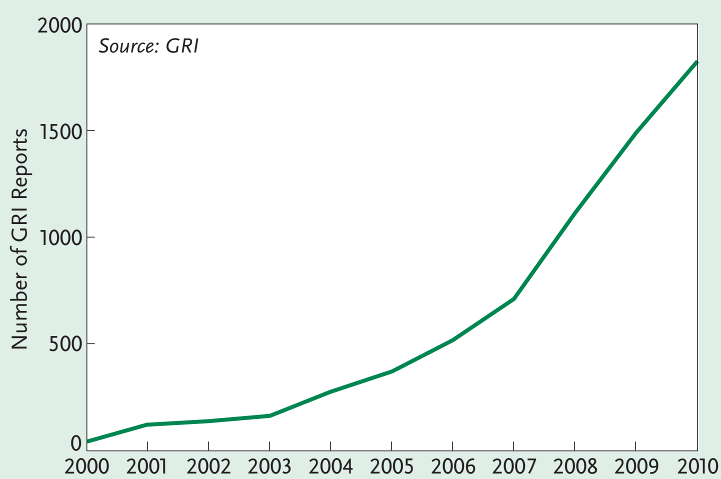


Notwithstanding its impressive expansion, the Compact has not been immune to criticism for shortcomings in accountability to the U.N. system, inadequate screening and monitoring of participants, and the absence of regular and independent performance monitoring. For example, not until 2004 was a process for "delisting" participants put in place to deal with any failures to prepare the required Communication on Progress (COP). Steady improvement has elevated COP compliance to approximately 76 percent in 2008, a respectable but still flawed level of adherence to the Compact's rules of governance.[11]

A second, kindred effort is the Global Reporting Initiative (GRI). Conceived in 1997

by two U.S. nongovernmental organizations (NGOs)—CERES in partnership with the Tellus Institute— GRI was launched in 2002 at the United Nations as an independent, nonprofit organization affiliated with the U.N. Environment Programme and dedicated to advancement of sustainability reporting by companies worldwide. Approximately 2,000 companies worldwide are registered as users of the GRI Guidelines and countless others do so informally. (See Figure 7-3.)[12]

Figure 7–3. Growth in Global Reporting Initiative Reports, 2000–10



As the GRI is adopted more widely, its influence can be seen in dozens of policies, regulations, and programs worldwide. Examples include the Swedish mandate that all state-controlled companies publish GRI-based sustainability reports, the alignment of sustainability performance indicators in the 2011 German Sustainability Code produced by the German Council on Sustainable Development with indicators of the GRI Guidelines, and the listing requirement on the Johannesburg Stock Exchange that corporations comply with the King Code of Corporate Governance, which embraces the GRI framework. Examples of this nature are indicative of a gradual evolution from soft law to semi-mandatory to full-fledged hard law. It is an evolution repeated often in the history of social change, as seen in the suffrage, environmental, women's, and anti-apartheid movements. In all cases, government shifts from observer to participant to codifier of emerging norms whose impulse originates outside of government itself.[13]

Like the Global Compact, GRI is both a reflection and a driver of new norms of corporate behavior. Until its creation, corporate disclosure of environmental, social, and nonfinancial economic impacts was seldom practiced. A handful of firms did so without rules, standardization, or, by and large, credibility. Disclosure initiatives were proliferating throughout the 1990s, advanced by business associations, companies, governments, and NGOs, but they were doing so without an overarching, generally accepted framework built on a core set of principles, processes, and indicators.[14]

In little more than a decade, GRI has been a major force in moving the practice of sustainability reporting from the extraordinary to the exceptional to the expected. In 2013, GRI will release the fourth generation of its Guidelines. Perhaps a half decade hence, sustainability reporting may be blended seamlessly with financial reporting to create a single, "integrated reporting" framework. Meanwhile, the collective experience of thousands of reporters during the last decade is providing the necessary data for investigating the critical but elusive question: Apart from the intrinsic good associated with greater transparency and accountability, is sustain-

ability reporting driving positive change in terms of fair wages, reduced carbon emissions, ethical advertising, and other dimensions of the corporate sustainability agenda? Research during the next few years will shed light on this pivotal question.[15]

Soft law in this field also covers scores of initiatives on specific sectors. SA 8000 on decent work standards overseen by Social Accountability International (SAI), the Marine Stewardship Council, and the Forest Stewardship Council are multistakeholder global efforts seeking to redefine the rules of acceptable corporate conduct, practices, and products. Like the Compact and GRI, these initiatives saw steady expansion during the last decade, measured in terms of certified factories, fisheries, and forest areas.

While progress among voluntary initiatives is undeniable, so too are the limitations. The Compact's 6,000 corporate endorsers, GRI's 2,000 reporters, and SAI's 2,300 facilities are but a tiny fraction of the tens of thousands of TNCs, millions of small to medium-size enterprises, and countless factories in the global economy.[16]

Stepping back from individual initatives, the aggregate evidence provides little reason to believe that voluntarism alone is capable of shifting corporate practices at a pace and depth commensurate with the challenges that lie ahead. The bubbles and busts in technology and housing markets throughout many industrial nations, the financial meltdown of 2008 and ensuing recession, intensifying stress and ominous signs of irreparable damage to the biosphere—all these point to an urgent need to move beyond voluntary initiatives and piecemeal, issue-specific, company-driven improvements. Advances in reducing carbon emissions, upgrading supply chain management, and strengthening worker health and safety are noteworthy. But they are no substitute for systemic change that can only occur through deeper reflection centered on the nature of the corporation and the roots of conditions that stand in the way of tapping the corporation's full potential as an agent of sustainable development.

Creating a plausible and inspiring vision of the new corporation requires a set of framing principles and living examples of how such transformative changes would actually look. Such a vision is part and parcel of many current efforts to envision a hopeful planetary future rooted in the values of stewardship, justice, and solidarity on the part of individuals and the institutions that serve them. (See Box 7–2.)[17]

Vision

Imagine the following scenario: In 2015, after years of quiet deliberation and coalition building, an alliance of global business leaders forges an improbable coalition with civil society and labor organizations. Under the relentless pressure of deepening wage and wealth inequalities and intractably high unemployment, and facing an insurgent global citizens movement fueled by a sense of disempowerment and enabled by social networking technology, the alliance steps forward to say:

> We are here to declare that business-as-usual is not an adequate response to the expectations, risks, and opportunities for corporations in the twenty-first century. We therefore are advocating a change in the rules governing corporations, a new social contract that recognizes that companies exist at the pleasure of citizens expressed through democratic government processes that provide the rule of law, the stability, and the physical and technological infrastructure upon which all companies depend. The mantra of shareholder value is antithetical to the core values of sustainable development, which is the only long-term pathway to build the prosperous companies and prosperous societies upon which our collective well-being depends.

Box 7–2. Envisioning Sustainable Futures

What will communities and economies look like in the future? Where will current sustainable development policies take the world, if implemented? Most important, what does success look like, if humanity gets things right? The positive vision question is often missing in sustainability discussions, and it is a key reason why shared strategic action is so challenging. Yet as systems thinker Donella Meadows once said, "Vision is the most vital step in the policy process. If we don't know where we want to go, it makes little difference that we make great progress. Yet vision is not only missing almost entirely from policy discussions; it is missing from our whole culture."

When done well, visioning can be very effective, as it both catalyzes creativity and enables people to be far more strategic. The strategic power of visioning lies in how it moves beyond a fragmented, short-term, incremental, and narrow approach. Techniques like scenario planning allow a review of the consequences of the current trajectory and alternative pathways. Having stakeholders think together about the future—an open space still undetermined and thus less burdened by past differences, grievances, and assumptions—makes it easier to reframe stuck debates, build a shared understanding of emerging realities, and identify common interests. Cities like Detroit, countries like South Africa, and companies like Cisco are all using these collaborative visioning processes to transcend deep divides, create new innovative breakthroughs and strategic flexibility, and discover how to co-design a better shared future for all.

The process of creating a vision draws on the creativity of those involved. Advancing sustainability requires envisioning not only possible futures but positive and compelling visions of these futures. There are an increasing number of initiatives aimed at filling this visioning gap, from the World Business Council on Sustainable Development's Vision 2050 report to the Great Transition Initiative. But supporting a global dialogue—from the grassroots to the mainstream—about the future is still a challenge. The engagement process needs to be deeper, wider, and richer in order to reimagine how humanity can work, live, and play together equitably on Earth.

The good news is that the future is not determined. The gift of foresight means people can anticipate, adapt, and create new alternatives. The negative scenarios can be avoided if people act wisely and boldly now. Indeed, humanity's long-term future as a species may depend on this.

—Nicole-Anne Boyer, Adaptive Edge
Vanessa Timmer, One Earth
Source: See endnote 17.

We commit to creating new global, national, and local governance mechanisms with the authority and resources to encourage and enforce a new generation of corporate accountability and adherence to a new set of principles for corporate design. These principles will provide the beacon for an emergent view of the corporation built on a partnership between people and the biosphere.

A decade ago, this scenario would have been implausible. But in the second decade of the twenty-first century, scrutiny of corporate behavior in both the finance and nonfinance sectors is at an unprecedented level. The volatility and systemic risks during the last decade have shed a harsh light on conduct in the financial sector. Failure to regulate banks' capital requirements properly, the proliferation of exotic and risky derivatives, and the social consequences of the co-mingling of commercial and investment banking activities all con-

spired to destabilize global financial markets. The widespread public sentiment that the concentration of profits and wealth in the finance sector is a distortionary and unjust force in global markets has corroded confidence in financial organizations and the government entities responsible for their regulation. This has fueled demands for remaking the finance sector to discourage or prohibit financial corporations from becoming “too big to fail” owing to the systemic risk they create in national and global economies. This new situation reflects the fact that the ultimate risk of failure is borne not by investors but by taxpayers of host countries and, in the case of the European Community, a whole region. In these circumstances, “too big to fail” is better characterized as simply “too big.”

At the same time, the nonfinancial corporations—the so-called real economy of goods and nonfinancial services—are not immune to diminished public confidence. In industrial countries, a deep and lengthy recession has undermined confidence in the capacity and will of corporations to look beyond the next quarter’s share price and earnings to invest in the future of the company, its employees, and the community in which it operates. The gradual “hollowing out” of manufacturing jobs and the threats to traditional safety nets in the United States, much of Europe, and Japan raise profound doubts about corporations’ capacity to share fairly the wealth they create among those responsible for its creation. The U.S. government’s bailout of the large corporations in the auto industry raised questions about whether such industries should be subject to the same leverage regulations (that is, borrowed debt) and restrictions as are applied to the banking community. And as major emerging economies such as China, Brazil, and India regularly report progress toward poverty alleviation, the contrast with the underperforming, job-deficient industrial nations becomes all the more stark.[18]

At least three conditions are likely to continue to erode public confidence and intensify pressure for change among TNCs: scale, transience, and disparities. First, scale. Unbridled growth continues to expand the market and the political influence of TNCs. Finance, autos, pharmaceuticals, the media, and food are among the sectors that have consolidated into small numbers of major global producers and service providers. The growth imperative, measured by share price, earnings per share, and short-term profits, induces business decisions of questionable societal value: ill-conceived acquisitions to bolster short-term profitability; creative accounting to inflate earnings, for example, through deferral of R&D and maintenance expenditures; executive compensation at historically high levels of disparity relative to median worker wages; and an overreliance on stock options that induces obsessive attention to short-term share price instead of long-term wealth creation. The result is widespread belief that too many TNCs, beholden to shareholder pressure and entrenched short-termism, are failing to contribute to the long-term well-being of workers, communities, and the environment at levels commensurate with their capacity to do so.[19]

Transience is a second driver of public disillusionment. In the era of computerized, high-frequency trading, share ownership that years ago was measured in months and years is now reduced to minutes and seconds. Transiency also is manifested in the behavior of footloose industries that continuously seek lower-cost production sites. Accountability to workers and communities has little role to play in this hyper-competitive transient global economy. While the system may yield quick returns to selected investors, the societal costs are severe in terms of diminished community cohesion and worker dislocation. For shareholders, transience is simply the contemporary expression of “creative destruction” that benefits stock traders and sophisticated investors in the name

of efficiency and competitiveness. For other stakeholders, the system has diluted the concept of "ownership" to the point where the corporation has become a tradable commodity (like petroleum, minerals, and grains), largely detached from the consequences of its actions on the lives and livelihoods of the communities and individuals where it operates.

Wealth disparities, a third driver of public disquiet with corporate behavior, has never been viewed as the responsibility, much less the outcome, of corporations operating in a free market environment. That role traditionally falls to government. Despite much rhetoric, sustainability issues—climate stability, human rights, poverty alleviation—struggle to attract the attention of both corporate executives and investors. Making the business case for pursuing such issues through investment strategy and portfolio management has made some progress in the last decade, but overall it remains at the margins of managers' and investors' calculus. The results speak for themselves in terms of persistent macro-level income disparities within and across nations, micro-level disparities in the form of the ratio of executive pay to average wages, and record corporate profits juxtaposed with stagnating or declining real wages of workers.

Creating the preconditions of transformational change requires general acceptance of new principles that confront and help reverse the injurious effects of scale, transience, and disparities. Fortunately, multiple initiatives are afoot—focused on both the "new corporation" and the "new economy"—that point to a future in which human and ecological well-being are the centerpieces of a movement toward a just and sustainable future.[20]

Principles

For more than five years Corporation 20/20—an international network with more than 300 participants from business, civil society, law, labor, and academia—has explored the challenges of repurposing and redesigning corporations. Bound by the belief that new models of corporations are indispensable ingredients for a healthy global future, the network developed six Principles of Corporate Redesign as the pillars of its research, advocacy, and public communications. These principles provide an architecture for the next generation of corporations.[21]

- *Principle 1. The purpose of the corporation is to harness private interests to serve the public interest.* Why does society create laws that allow corporations to exist? To serve the public interest, the paramount purpose of all democratic systems. The license to operate is not an entitlement; it is a privilege. It should be granted with terms and conditions aligned with the vision of a just and sustainable society and be subject to periodic review and renewal based on adherence to such vision. This principle recognizes and reinforces the unique capacity of the corporation to generate wealth. At the same time, it insists that in the process of wealth creation, the corporation must act in a manner consistent with the public interest. Where private and public interests conflict, the public interest must prevail. Principle 1 rejects the characterization of the corporation as an insular entity freely marketable without constraints and detached from the broader society in which it operates. Instead, it positions the corporation as inseparable from, and ultimately accountable to, broader societal interests.
- *Principle 2. Corporations shall accrue fair profits for investors, but not at the expense of the legitimate interests of other stakeholders.* Profit and investment are vital to a well-managed corporation. But they are means, not ends. Corporations may not pursue profit for shareholders by undermining the legitimate interests of other stakeholders. The word "legitimate" is critical because claims vary according to the contribution of various

stakeholders to the corporate value creation process—specifically, as providers of human, natural, social, and financial capital to the corporation. In the course of corporate activity, off-loading external effects onto society is fundamentally at odds with the public interest. It shall be deemed unacceptable and avoided through appropriate policy and regulatory mechanisms.

- *Principle 3. Corporations shall operate sustainably to meet the needs of the present generation without compromising the ability of future generations to meet their needs.* Vital to the public interest—and vital to human and ecological well-being—is the stewardship of the biosphere through the preservation of natural resources and protection of common assets such as clean air, water, and the Earth's climate. This principle states unequivocally that corporations have intergenerational responsibilities. Managing for short-term private gain is a violation of such responsibilities. Operating sustainably implies a dramatic change in the nature and production of goods and services and the incorporation of the true cost of such production throughout the value chain.
- *Principle 4. Corporations shall distribute their wealth equitably among those who contribute to its creation.* This principle positions equitable wealth distribution as an explicit, though not exclusive, responsibility of business. It rejects prevailing norms of corporate governance and fiduciary duty that make shareholder wealth paramount and the wealth of all other recipients subordinate. Gains to other stakeholders—wages for employees, payments to suppliers, and taxes to local and national governments—currently are defined as costs to be minimized in deference to the primacy of shareholder interests. In contrast, a corporation design aligned with Principle 4 recognizes its obligation to share the wealth it creates equitably among all parties that contribute to it, including payments to government whose provision of stability, security, and the rule of law are indispensable to successful business operations.
- *Principle 5. Corporations shall be governed in a manner that is participatory, transparent, ethical, and accountable.* Participatory governance empowers stakeholders at all levels of corporate decisionmaking. Through governance structures that are transparent and accountable, affected parties are informed, heard, and influential—conditions that nurture productivity, loyalty, and cohesion in the organization. "Stakeholder governance" of this nature is closely intertwined with all other principles. When designed effectively, it is a mechanism for embedding democratic, participatory principles into corporate governance while ensuring that management retains the discretion to operate the organization competitively and efficiently.
- *Principle 6. Corporations shall not infringe on the right of natural persons to govern themselves, nor infringe on other universal human rights.* This principle speaks to the corporation's relationship with the broader political rights of citizens. It delineates a boundary that corporations shall not transgress—namely, the rights of natural persons to govern themselves through delegation of certain rights to government for the benefit of the public interest. Corporations shall not exceed their proper role in democratic political processes and shall respect norms that limit their influence in lawmaking when such influence dilutes or suppresses the voice of the citizenry.

Collectively, these six principles provide the underpinnings of a new corporation whose purpose and design is aligned with the 2015 vision described earlier. The notion that corporations are chartered by governments to serve the public interest harkens back to an earlier era when all corporations—whether royally chartered in the sixteenth century to conduct global trade or state-chartered in the nine-

teenth to build a road or canal—functioned as time- and scope-limited public purpose entities. It is neither plausible nor necessary to turn the clock back centuries to reconstitute the historical corporate form. But it is both plausible and necessary to rethink such forms in ways that align with the perils and imperatives of inhabiting a sustainable planet in the twenty-first century. That challenge, in turn, requires application of these six principles to key levers of change critical to shaping the corporate "DNA" in the coming decades.

Levers of Change

Corporations are not islands. They are part of a complex economic system with a multitude of simultaneous variables continuously shaping and reshaping their performance. The four dimensions of change described here point to the multiple pathways through which transformational change is possible.

Purpose. Through both legal (charter and bylaws, for instance) and extra-legal (mission statement or family legacy) means, a corporation's statement of purpose both reflects and reinforces its moral fiber. Purpose serves as a touchstone when critical governance, strategy, and policy decisions are on the line. It also serves as a window into the mind of the organization and the degree to which its commitment to creating societal benefit in addition to private wealth is embedded into organizational culture. When the *New York Times* and Novo Nordisk define their purposes, respectively, as "inform the electorate" and "defeat diabetes," it is a signal that social mission plays a significant role in shaping company culture and, ultimately, strategy and management practices.[22]

Countries vary widely in their requirements for organizations to explicitly state their purpose in their bylaws or charter process. In no case, however, is the charter process aggressively deployed as an instrument to advance a country's sustainability agenda. Countries with common law traditions—such as the United Kingdom, the United States, Canada, and Australia—do not legally require a statement of purpose. In contrast, those with civil law traditions typically do, including Germany, France, Italy, Spain, Brazil, and Chile. But even in the latter cases, a declaration of purpose generally means purpose within the context of the business sector in which the firm operates—for instance, "the purpose of company X is to produce pharmaceuticals for institutional and consumer markets."

Recent U.S. developments point to the possibility of a new generation of state charter options that foster a broader, stakeholder-centric statement of purpose. One example is the B Corp (B for benefit), a voluntary alternative to traditional value-free charters that allows companies to use charter language to explicitly recognize the interests of community, workers, the environment, and other non-shareholder stakeholders in operating the organization. B Corps are required to have a corporate purpose to create a material positive impact on society and the environment, to redefine fiduciary duty to require consideration of the interests of employees, community, and the environment when making decisions, and to publicly report annually on their overall social and environmental performance using a comprehensive, credible, independent, and transparent third-party standard. Hawaii, Maryland, Vermont, New Jersey, Virginia, and California have enacted legislation on B Corps as a voluntary alternative to existing shareholder-centric charters, and other states are considering such action. More than 400 companies, mainly start-ups and small organizations, representing over $2 billion in revenue, have been certified as B Corps.[23]

A second charter innovation is California's Flexible Purpose Corporation (FPC), enacted in October 2011. This law aims to provide corporations with a legal framework that protects and encourages a social mission but with a

more robust protection of corporate directors from shareholder lawsuits than that contained in B Corp laws. The FPC enables directors to consider the long- and short-term interests of shareholders, employees, suppliers, customers, creditors, community, society, and the environment. Advocates of FPC hope that the new law will attract larger corporations than those drawn to B Corp status by fostering possibilities for mainstream business to blend private and societal wealth creation.[24]

As an instrument for accelerating corporate transformation, charter law is an underused tool. The B Corp and FPC merit the attention of policymakers and regulators in emerging economies at a time when new business formation is accelerating rapidly and the entrenched shareholder-centric fiduciary laws are far weaker than in industrial countries. In emerging economies, charter law could be strengthened by a number of changes aligned with B Corp content: mandatory statement of a public purpose, periodic review of the company's adherence to such purpose as the basis for charter renewal, and mandatory sustainability reporting to disclose specific progress in meeting its self-declared social mission.

Is the spirit of B Corp and FPC transferable to the global stage on which TNCs operate? Yes, it can be and should be. TNCs are global enterprises and, as such, should be subject to enforceable global governance mechanisms much like international trade, international intellectual property rights, and protection of the biosphere (through the Montreal Protocol) already are. A recent proposal for creation of a global chartering entity for TNCs, the World Corporate Charter Organization, offers one approach to achieving congruence between the reach and governance of TNCs. The proposed global charter would complement rather than supplant national charters and would be granted for 10 years. Renewal would be subject to review and confirmation of a TNC's adherence to its charter obligations. A typical global charter would have five parts: a social mission, international norms, an ownership component, a governance section, and an accountability section. Chartering global enterprises at the national or state level represents a fundamental misalignment of purview and regulation that can be rectified only by such a global governance body.[25]

Ownership. Ownership, like purpose, plays a pivotal role in shaping and reinforcing the worldview of the corporation. Many alternatives to the dominant western ownership model of the joint stock, limited liability corporation—such as trust ownership, employee ownership, cooperative ownership, and community-based, hybrid social enterprises—are generally better aligned with the principles of corporate design described earlier.

Such corporate forms readily mesh well with concepts such as stakeholder governance, fair distribution of wealth created by the enterprise, and orientation to long-term horizons. Moreover, such forms are not curiosities. They in fact exist by the thousands in numerous countries, though their prominence is seldom tied to broader debates surrounding business-society relations. In the United States alone there are some 11,000 totally or partially employee-owned companies and 130 million members of urban, agricultural, and credit union cooperatives. In Europe, over 300,000 cooperative businesses employ 5 million people. In Spain, the Mondragon cooperative in the Basque region is a prosperous, umbrella entity with 100,000 employees in a wide range of product and service enterprises. In Italy, the Lombardia region counts over 11,500 cooperatives and 170,000 related employees. And in the United Kingdom, the John Lewis Partnership—a $10-billion, employee-owned enterprise with some 70,000 employees—is the largest department store chain in the country. Annual profits are for the most part distributed among staff members, who are, in effect, the shareholders of the organization.[26]

Contemporary ownership structures are unduly wedded to nineteenth-century industrial capitalism, an era of capital scarcity and labor and natural resource abundance. In the twenty-first century, where financial capital is plentiful and skilled human capital and natural capital are relatively scarce, alternative ownership structures are flourishing and in a constant state of reinvention. The Grameen Bank/Groupe Danone (Bangladesh/France) joint venture exemplifies a new generation of blended business models that have at their core a social purpose—in this case, affordable nutrition for Bangladeshi children through the manufacture of fortified, low-cost yogurt. Meanwhile, trust- and foundation-controlled companies answer to a higher purpose defined by the nonprofit entity that holds controlling shares. Novo Nordisk (Denmark), GrupoNueva (Chile), and Tata Industries (India) fall into this category. In the case of Tata, 90 enterprises are controlled by family trusts and bound by the 140-year-old legacy of its founder to advance social capital.[27]

The Chinese model of state capitalism is yet another ownership model: the principal stakeholder typically is also the principal shareholder—China itself. The rise of Chinese enterprise worldwide in sectors such as mining, automobiles, and computer technology is moving the country well beyond the boundary of low-end manufactured goods into becoming a global player in both low and high technology. Here, enterprises are as much social and political instruments as they are economic engines, fortifying China's effort to ensure secure flows of minerals and food commodities from African and South American sources. Internally, such ownership is used as an instrument to foster social harmony, reduce inequalities between coast and interior communities, and accelerate the rise of the middle class—critical elements of the country's social agenda. Of course, the intimate connection between government and state enterprise has serious downside risks, whereby enterprises are beholden to political control aimed at preserving the one-party system. The scale of ecological degradation in China attests to the dark side of state capitalism, when political and economic interests trump environmental protection—to the long-term detriment of China's public health and ecological resilience.

All these examples illustrate the broad spectrum of ownership options in play on the world stage. To varying degrees, by design or by consequence, each provides an alternative to the dominant western model in terms of alignment with vision and principles of the new corporation depicted here. In an interconnected world confronting multiple ecological, economic, and social crises, ownership stands as one of the powerful pressure points for rethinking corporate designs such that they ingrain social mission in the conduct and culture of contemporary enterprises.

Capital. Whatever purpose or ownership structure is in place, corporations need financial capital to launch and sustain their operations. The access, sources, quantity, and conditions by which investment occurs play a pivotal role in enabling or impairing the transformation envisioned here.

Historically, capital markets have been at best indifferent to the long-term social consequences of investment practices. Among the tens of trillions of dollars in assets under management worldwide, only a small fraction is subject to any form of screen that aligns with the principles of the new corporation. In the United States, for example, recent estimates place the figure at $3.1 trillion, less than 15 percent of total assets under management.[28]

Globally, a number of the world's 100 stock exchanges are taking steps toward bringing sustainability into their listing requirements or other mechanisms for informing investors of the materiality of sustainability to their decisionmaking. These include the Shanghai Stock Exchange, BOVESPA (São Paulo), Johannesburg Stock Exchange, Deutsche Börse, Sin-

gapore Exchange, and the Stock Exchange of Thailand. At the same time, spurred largely by GRI, sustainability disclosure initiatives with capital markets as a key target continue to proliferate worldwide. By one estimate, some 142 standards or laws are in place, with two thirds of them mandatory. A portion of these are related to capital market activity, reinforcing the view that sustainability is moving, albeit slowly, from the margins into the mainstream of financial markets and government policy.[29]

Outside of the mainstream capital markets that traditionally serve public equities is a new asset class commonly referred to as "impact investing." Spurred by a coalition of 15 foundations seeking to harmonize their investment portfolios with their programmatic goals, together with a number of mainstream firms serving mission-oriented clients, impact investors seek opportunities in start-ups, funds, social enterprises, and projects for which social value is the central goal. Principally targeted at emerging markets and poor countries, the coalition represents \$1.5 billion in assets aligned with impact investment performance metrics developed by an affiliated initiative, the Global Impact Investment Rating System. In the context of the new corporate designs, assets of this nature could become significant if they expand from their current modest level to, say, a trillion dollars or more in the next 5–10 years. In a similar vein, the Global Initiative for Sustainability Ratings seeks to reach beyond the relatively small mission-oriented investment community to drive environmental, social, and governance impacts into the mainstream capital markets.[30]

A future in which sustainability becomes seamlessly woven into the fabric of capital markets is a future with great promise for creating and expanding sustainability-oriented corporate forms. Realizing this potential at the magnitude and speed warranted by multiple global crises will require government actions in relation to securities regulation and stock exchange rules, public financing mechanisms in the form of national and state banks and targeted subsidies for new mission-oriented corporations, fiduciary regimes friendly to mission-driven investors, and capital gains taxes that privilege such investors. Examples of these types of actions are already in place. A vast scaling up and scaling out should be part of the Green Economy agenda of Rio+20 and beyond.

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Governance. To accelerate corporate transformation, corporate governance—the structure of decisionmaking and accountability in an organization—must shift from a focus on shareholder accountability to stakeholder accountability. Governance structures and processes that operate with a broader, integrated view of the nature, sources, and equi-

table distribution of corporate wealth creation are the same structures and processes that best align with the desired corporate purpose and design. Central to transitioning to such a stakeholder paradigm of governance are the values, knowledge, and oversight of the board.[31]

Why, more than two decades after inception of the contemporary sustainability movement, does sustainability remain at the margins of the vast majority of TNCs? Shortcomings in corporate governance surely rank among the most powerful impediments. Owing to a combination of law, culture, and choice, the vast majority of corporate boards continue to embrace shareholder value as the ultimate measure of business success. Indeed, attachment to this pillar of governance has assumed something akin to the law of gravity—undeniable, uncontestable, and unchallengeable.[32] The primacy of capital interests permeates virtually every corporate national and international governance initiative.

U.N. Secretary-General Ban Ki-moon's indictment of the global economy is equally applicable to corporate governance: "The global economy needs more than a quick fix. It needs a fundamental fix. If we have learned anything from the financial crisis, it is that we must put an end to the unethical and irresponsible behavior and tyrannical demand for short-term profit."[33]

Transforming corporations to align with the principles of corporate design requires transformation of the boards that are responsible for organizations' long-term prosperity. The necessary values shift will take time and organizational will, legal and regulatory reform, a reorientation of global governance norms and standards, and, perhaps more decisively, pressure from stakeholders whose interests are underserved by current governance structures.

Illustrative actions that will contribute to this transformation are:

- requirements that all existing and future board members build their professional competence through training in governance for sustainability;
- reconstitution of boards to include a mix of directors whose background and expertise mirror the full spectrum of the organization's key stakeholders;
- creation and independent funding of a Futures Council, a body that independently assesses the board's and the company's sustainability performance with reference to the interest of all legitimate stakeholders, including those of future generations;
- a requirement that directors hold management accountable for integrating sustainability into all business functions, and regular monitoring and assessment of such integration; and
- integration of executive compensation with the company's sustainability performance.

No single action is a panacea for transforming corporate governance. Indeed, it can be argued that the durability and effectiveness of any measure must be preceded by a deep reflection on the part of directors as to the purpose of the corporation, the role of the board in achieving such purpose, and the meaning of duty of loyalty and duty of care in the twenty-first century. As the Brazilian Institute of Corporate Governance has noted, the most advanced stage of a board's evolution is when sustainability initiatives are not presented to a board—instead, they emanate from it.[34]

The Road Ahead

A decade ago, Charles Handy, among the most incisive contemporary observers of the modern corporation, asked the most fundamental of all questions: What's a business for? His response remains relevant today: "To turn shareholders' needs into a purpose is to be guilty of a logical confusion, to mistake a necessary condition for a sufficient one. We need to eat to live; food is a necessary condition of life. But if we lived mainly to eat, making food

a sufficient or sole purpose of life, we would become gross. The purpose of a business…is not to make a profit. Full stop. It is to make a profit so that business can do something more or better. That 'something' becomes the real justification for a business. Owners know this. Investors needn't care."[35]

The question of corporate purpose is central to the multitude of issues that define current debates over business-society relations. In Handy's terms, the "something" identified here is "the public interest"—which today translates into building a just and sustainable world. From this purpose flows the set of design principles, and from design principles flow the levers of change that are central to creating a generation of corporations that embed social mission in all aspects of their activities.

The seeds of such a transformation are discernible. Rio+20's focus on the Green Economy in the context of sustainable development and poverty eradication, one of two major conference themes, is but the latest evidence of this evolution.

A small but growing number of TNCs understand the imperative and the opportunity of revamping their business models to enhance both long-term value creation and competitiveness. Their leaders demonstrate the readiness to open a new chapter in business-society relations, to rewrite the social contract by bringing the commercial sector into the contract in a way that transparently, accountably, and democratically reinforces the historic bargain between citizens and their governments. Consumer goods TNC Unilever CEO Paul Polman, in advocating for the company's Sustainable Living Plan, argues: "Changes in policy will mean little if not accompanied by changes in behavior. That's why we need a different approach in business—a new model led by a generation of leaders with the mindset and the courage to tackle the [sustainability] challenges of the future." That "model" should be rooted in the vision, principles, and levers for change that are essential for repurposing and redesigning the corporation.[36]

In light of all these developments, the 2015 scenario described earlier does not seem as implausible as it might at first read. The building blocks, though scattered and imperfect, await bold and persuasive change agents from within and outside of the business community. Will history look back at Rio+20 as a moment when such agents boldly stepped forward with the will, passion, and determination to become the vanguard of transformation in the purpose and design of the corporation?

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